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## AT LAW

### Fighting Over the Balance Left on Unused Gift Cards

By JON HART and MELANIE HILL  
Special to THE WALL STREET JOURNAL ONLINE

U. S. merchants have grown quite fond of selling electronic gift cards. But their growing popularity has also raised the stakes for retailers when cards go unused.

As paper gift certificates are becoming quaint reminders of a bygone era, sales of electronic gift cards are soaring. They hit \$38 billion in sales in 2002, according to data presented at the annual conference of the National Association of State Treasurers; sales in 2003 are expected to be stronger still.

Gift cards have many advantages over old-fashioned gift certificates. They are cheaper to issue and administer than paper certificates, and sales and redemptions can be tracked electronically by store. Gift cards are also more secure because electronic gift cards that haven't been activated have no value -- whereas unissued paper gift certificates must be guarded from theft.

And gift cards, like their paper ancestors, are attractive to merchants for another reason: When redeeming a gift card, the average consumer spends considerably more than the value of the card. (Estimates range from 15% to as much as 40% more.) It's no surprise that major retailers, from Starbucks to Costco, have been aggressively promoting branded gift cards.

Gift cards have another potential benefit: According to ACS Unclaimed Property Clearinghouse Inc., roughly 10% of them are never redeemed. Given projected 2003 sales of \$45 billion, that's nearly \$5 billion in unclaimed gift card value. But whether a retailer is able to benefit from these unclaimed funds depends on so-called escheat laws, which govern custody of abandoned funds -- as well as how far the retailer is willing to go to avoid the reach of these laws.

So, are unused gift cards a gift to the retailer? Or are they a gift to the state?

Every state has laws that allow it to take custody of funds abandoned by its residents, to hold them until the rightful owner can be located. In the past, virtually every state regarded

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Bloc in an unredeemed gift card or gift certificate as unclaimed property if the owner didn't use the card within some number of years set by statute. Under those rules, if the issuing store has a record of the purchaser's name and address, it must attempt to contact the purchaser to alert him that the funds remain unused. If the store can't find the purchaser, the value of the unredeemed gift card is passed to the state of the purchaser's home or, if the address is unknown, to the state where the retailer is incorporated.

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Many retailers don't like these laws. When the state "escheats" an unused gift card, the retailer that issues the card is deprived of the profit it expected to earn when the card was redeemed for merchandise. The retailer actually loses money on the gift card because it has to cover the expense of issuing and accounting for the card, but turns the value of the card over to the state. Retailers used these arguments, with some success, to lobby for changes in these laws. About half the states no longer claim the value on gift cards or claim only a portion (such as 60%) of the value of an unused gift card. But other states have adamantly refused to acknowledge retailers' concerns and claim the full sales price of unused gift cards.

Some retailers have also tried to protect gift-card profits by imposing conditions on gift cards, such as expiration dates or monthly service fees that whittle away the value of the gift card. That way, it has no value by the time the state would otherwise claim the value of the unredeemed card.

But expiration dates that diminish the value of gift cards are unpopular with consumers. And many states, including California, Connecticut and Massachusetts, have passed legislation that prohibits the imposition of an expiration date or service fees. Sen. Charles Schumer (D., N.Y.) plans to introduce federal legislation next month to regulate gift-card fees.

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#### Retailers Shop for a Forum

These legislative responses to gift-card fees have prompted a counter-solution from retailers; in the holiday spirit, the solution involves shopping. Retailers are forming separate gift-card companies to sell and redeem their electronic gift cards and are "shopping" for the best state in which to form these new companies. Though many large retail chains are incorporated in Delaware, which actively seeks to claim gift-card balances, the new gift-card subsidiaries are being formed in states with friendlier policies toward retailers.

So, whom to root for in this game of cat and mouse? The answer might depend on your view as to who is in a better position to protect consumers' unused property: retailers or the state. Certainly, as long as retailers continue to impose service fees, states will take the position that retailers aren't adequately

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protecting consumers, and, like Massachusetts, California, and Connecticut, may pass laws to prohibit fees or to require that the full value of the unredeemed gift card be turned over to the state.

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However, it is less likely that states will aggressively claim gift cards if retailers move to protect consumers by eliminating these fees. And, it seems to assume that consumers are more likely to recover unused gift-card funds from a retailer looking for repeat business than from a government agency in some far off state.

The electronic card industry is still young, and some of these disputes may be resolved. For instance, the separate gift-card companies may well benefit from technological advances and economies of scale similar to those gained in the consolidation of the industry. As retailers look to issue cards that track customer purchases and allow them to target their promotional campaigns, the gift-card companies will need to record the address of the purchaser or gift recipient.

Already, some retailers are issuing gift cards that consumers can register so that they can be issued if the original is lost before it is used. More broadly, with this contact information, gift cards may never become unclaimed property eligible to be escheated; retailers will have an address to contact the owner of the card.

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